IN THE

Supreme Court of the United States

OCTOBER TERM, 1976

76-1580

In the Matter of the Application of
SANDS POINT NURSING HOME,
Petitioner,

against

HOLLIS S. INGRAHAM, as Commissioner of Health of the State of New York and RICHARD L. DUNHAM, as Budget Director of the State of New York,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE STATE OF NEW YORK

RESPONDENTS' BRIEF IN OPPOSITION

LOUIS J. LEFKOWITZ
Attorney General of the
State of New York
Attorney for Respondents
Office & P.O. Address
Two World Trade Center
New York, New York 10047
Tel. No. (212) 488-6770

SAMUEL A. HIRSHOWITZ
First Assistant Attorney General

AMY JUVILER
Assistant Attorney General
of Counsel

TABLE OF CONTENTS

	PAGE
Opinions Below	1
Jurisdiction	2
Statute Involved	2
Statement	3
Reasons for Denying Certiorari	6
I. The decisions of the Court of Appeals and Appellate Division are clearly correct	6
II. No important constitutional issues are presented in this petition	10
III. The decisions below were based on the particular facts of this rate fixing and are not likely to recur	11
Conclusion	12

TABLE OF CASES

Arizona Grocery Co. v. *Atchison, Topeka & Santa Fe Ry. Co.*, 284 U.S. 370 (1932)	10
Great Northern Ry. Co. v. *Sunburst Oil & Refining Co.*, 287 U.S. 358 (1932)	10, 11
Matter of 225 E. 70th St. Corp. v. *Weaver*, 6 N Y 2d 197, 189 N.Y.S. 2d 153 (1959)	9
Matter of Sigety v. *Ingraham*, 29 N Y 2d 110, 342 N.Y.S. 2d 10 (1971)	8
United States v. *R.C.A.*, 358 U.S. 334, 79 S. Ct. 457, 3 L. Ed. 2d 354 (1950)	9

Statutes Cited	Page
Public Health Law § 2801-a	8
Public Health Law § 2807 [3]	3, 6, 8, 11
New York Public Health Law § 2807(3)	2
L. 1972 c. 918 § 8, eff. April 1, 1973	3
L. 1976 c. 938 § 6, eff. July 27, 1976	3
10 N.Y.C.R.R. § 82.21	8, 11, 12
10 N.Y.C.R.R. § 86.24	7, 11, 12
10 N.Y.C.R.R. § 86.29	11
10 N.Y.C.R.R. § 86.32	5, 11, 12
10 N.Y.C.R.R. § 600.1	8
CPLR § 1019	5
§ 1023	5
§ 5511	5
42 U.S.C. § 1396b	7
§ 1396d	7

Miscellaneous

CCH Medicaid and Medicare Guide ¶ 4681, pp. 1641-3	4, 7
Medicaid and Medicare Provider Reimbursement Manual, § 104.14	7

In the

Supreme Court of the United States

OCTOBER TERM, 1976

76-1580

In the Matter of the Application of
Sands Point Nursing Home,

Petitioner,

against

Hollis S. Ingraham, as Commissioner of Health of the State of New York and Richard L. Dunham, as Budget Director of the State of New York,

Respondents.

On Petition for a Writ of Certiorari to the Court of Appeals of the State of New York

RESPONDENTS' BRIEF IN OPPOSITION

Opinions Below

The February 10, 1977, decision of the New York Court of Appeals which this Petition seeks to review is reported at 41 N Y 2d 837 (1977). It affirmed the decision of the Appellate Division, Second Department, which is reported at 48 A D 2d 897 (1975). The Appellate Division had dismissed petitioner's Article 78 petition on the merits and confirmed the determination of respondent the Com-

missioner of Health of the State of New York. In so doing it unanimously reversed the decision of the Supreme Court, Nassau County (MEADE, J.), entered on December 4, 1973, granting the petition in part. That decision is not reported, but is reproduced at pp. 10a, *et seq.* of the Petition.

Jurisdiction

The jurisdictional facts are set forth in the Petition.

Question Presented

Whether in setting the Medicaid reimbursement rate for the Sands Point Nursing Home, the Commissioner of Health was required to use the purchase price as the value of the property, even though he had determined that that was an unreasonably high value when no statute or regulation required that method?

The Appellate Courts below answered "No" as the respondents had contended and reversed the decision of Special Term which had held that the Commissioner was required to use the purchase price as the basis for the reimbursement rate.

Statute Involved

New York Public Health Law § 2807(3) as it existed at all times relevant to these proceedings provided in pertinent part:

> "Prior to the approval of such rates, the commissioner shall determine and certify to the superintendent of insurance and the state director of the budget that the proposed rate schedules for payments for hospital and health-related service are reasonably related to the costs of efficient production of such service."

In 1972 (L. 1972 c. 918 § 8, eff. April 1, 1973) and in 1976 (L. 1976 c. 938 § 6, eff. July 27, 1976) the language was changed but not to affect the standards quoted above.

Statement

This petition involves a determination of the property component of the Medicaid reimbursement rate for one nursing home. The rate was found to be "reasonably related to the costs of efficient production" (Pub. Health L. § 2807[3]) of nursing home services by two appellate courts of the State of New York based on the particular facts of the case.

This standard is fair and in conformity with the Constitution of the United States.

The question enumerated as "3" in the petition (Pet'n., p. 3) whether the determination of property costs by using appreciated value of property depreciated over its life violated the federal Social Security Act was not raised in the petition filed under Article 78, New York Civil Practice Law and Rules, in its brief in the courts below or ruled on by those courts. Quite the contrary, it was respondents who consistently have relied on Federal regulations to support the reasonableness of the rate setting in this case (see p. 7, *infra*).

The Sands Point Nursing Home was built in 1965 and in 1970, subject to straight line depreciation of 2½% a year, was valued at $508,943.00 (92 [p. 9*]). In that year the property costs were determined to be $117,714 or roughly $900 per bed per year (92 [p. 17]). Almost 50% of the net revenue from services to patients in the 6-month period ending June 30, 1970 was from private patients (92 [p. 16]).

---

* Unless otherwise designated numbers in parentheses refer to pages of the Record on Appeal submitted in the courts below.

Effective June 30, 1971, the facility was sold to the partners who presently own it for $2,145,000 (94 [p. 4]). The establishment of the Nursing Home by the new owners was approved by the Public Health Council (94).

On August 20, 1971, petitioner sought a revision in the property cost component of the Medicaid reimbursement rate on the basis of the purchase price of the facility at a rate of $260,375 per year or an average annual rate per bed of $2,000 (29-30). Because this was such an enormous increase of costs over the previous year and because the Commissioner determined that the purchase price reflected value other than the tangible assets, he made an independent evaluation of the property costs, using the recognized method of determining the value of the building by taking the reproduction cost less accumulated depreciation. See CCH Medicaid and Medicare Guide ¶ 4681, pp. 1641-3. The fair return on that property was found to be $143,000 a year or about $1,100 per bed (32-4). While lower than the $2,000 per bed rate sought by petitioner, this cost represented an increase of 22% over the property costs of the previous year (92 [p. 16]). The new rate was made retroactive to July 1, 1971 when the new property costs accrued.

Petitioner's objections were rejected by the Commissioner on August 28, 1972 (32-6, 37-8, 40).

Petitioner sought review of the Commissioner's decision by way of an Article 78 proceeding brought in the Nassau County Supreme Court. On October 5, 1973, Justice Meade issued his opinion which found that petitioner had contemplated that he would be reimbursed for the "actual property costs," i.e., the purchase price and that the Commissioner used a different rate. The Court rejected the rates established and required the Commissioner to establish a "proper rate" (13). The Court also stated that the Commissioner of Health revised the reimbursement rate on March 1, 1972, effective July 1, 1971* "and this he couldn't do" (12). The court did not declare 10 N.Y.C.R.R. § 86.32 to be void as petitioner had claimed, because its effective date was a month after the purchase of the facilities and was therefore inapplicable to the rate at issue (12-13).

The Appellate Division, Second Department reversed the judgment (150) on June 23, 1975, in a unanimous decision which held (154):

> ". . . the Medicaid reimbursement rate . . . fixed by the appellant State Commissioner of Health for the new owner's property cost factor was authorized and consistent with the mandate of subdivision 3 of section 2807 of the Public Health Law, which provides that rates be 'reasonably related to the costs of efficient production of such service.' That determination was reasonable, was authorized by statute, and should not be disturbed (*Matter of Sigety* v. *Ingraham*, 29 N Y 2d 110, 324 N.Y.S. 2d 10, 272 N.E. 2d 524)."

On February 10, 1977 the Court of Appeals affirmed the decision (FUCHSBERG, J., dissenting) 41 N Y 2d 837 (1977).

Early in 1975 Robert P. Whalen became Commissioner of Health and Peter Goldmark, Budget Director. Pursuant to CPLR §§ 1019, 1023, 5511 they were automatically substituted as respondents in the Court of Appeals.

---

* The rate had been at $900 per bed under the prior owners. The revision was sought by petitioner on August 20, 1971 (29-30). Had the rate not been revised retroactively petitioner would have received a $900-per-bed reimbursement for property costs for the period between July 1, 1971 and March 21, 1972 rather than $1100 a bed.

Reasons for Denying Certiorari

I.

The decisions of the Court of Appeals and Appellate Division are clearly correct.

In exercising his authority under Public Health Law § 2807(3) the Commissioner determined that the property cost reimbursement sought by petitioner was not "reasonably related to the costs of producing [nursing home] service" (Public Health Law § 2807[3]). By any measure, the Commissioner's determination was itself reasonable and should not be disturbed.

The cost increase sought by petitioner for the same service was 122% or from $900 per bed per year to $2,000 per bed per year. This increase is unreasonable on its face. There were no improvements to property to warrant such an increase in costs.

The rate of property cost reimbursement sought by petitioner was based on the total purchase price for the facility when that price obviously paid for more than the tangible assets represented in the property cost—good will and anticipated increased revenue from both private and Medicaid patients. It would be unreasonable for the Commissioner to have allowed the price for intangible profit producing assets to be included in property costs. Those relating to private patient revenue are irrelevant and those relating to Medicaid patients would become self-fulfilling prophecies of ever higher Medicaid costs (86-7).

No statute or regulation required the Commissioner to use the purchase price as the value of the property. Petitioner's request for a rate revision was not related to increased "costs of efficient production of such service," the statutory standard (Public Health Law § 2807[3]). Since those services had been produced for less than half the cost

the year before, petitioner cannot claim to be efficiently producing the services. The regulation in effect at the time (former 10 N.Y.C.R.R. § 86.24) provided:

> "Necessary interest on both current and capital indebtedness is an allowable cost for all medical facilities."

The use of the word "allowable" belies any reasonable reliance on an anticipated rate based on actual purchase price. There is no requirement that it must be allowed.

The cost basis employed by the Commissioner was one recognized by the regulations of the United States Department of Health, Education and Welfare (HEW). HEW set property costs as the lowest of three values: the purchase price, fair market value or the current reproduction cost depreciated over its life. Medicaid and Medicare Provider Reimbursement Manual, § 104.14; CCH Medicaid and Medicare Guide ¶ 4681, p. 1641-3:

> "The cost basis of a facility acquired as an on-going operation in a bona fide sale on or after August 1, 1970 is limited to the lowest of the following: (a) fair market value of the tangible assets purchased, (b) price paid by the purchaser (i.e., actual cost) or (c) current reproduction cost depreciated on a straight-line basis over the useful life of the assets to the time of sale."

Here, the Department used the third method, the reproduction cost. This also disposes of petitioner's belated assertion that the methodology employed by the Commissioner violated the Social Security Act.

Since HEW reimburses the State for a least 50% of the costs of Medicaid (42 U.S.C. § 1396b, 1396d), it is to be expected that their guidelines will be referred to by the Commissioner in determining Medicaid reimbursement rates.

On August 8, 1971 the Commissioner formalized his reliance on HEW's regulations (10 N.Y.C.R.R. § 86.21):

> "Allowable costs. (a) Except as otherwise provided in these rules, allowable costs will be determined by the application of the principles of reimbursement developed for determining payments under the Title XVIII (Medicare) program."

Petitioner had no right to rely on the Commissioner's prior practice of using the purchase price as the property cost basis in arms length transactions, since he was not required to use that figure.

In upholding the Commissioner's actions, the courts below were following established precedent that the Commissioner was not bound by past practice, if he established rates according to the statutory standards of reasonableness, e.g. *Matter of Sigety* v. *Ingraham*, 29 N Y 2d 110, 342 N.Y.S. 2d 10 (1971).

Petitioner claims that new limits on property costs were being applied retroactively. However, the Commissioner always had the power to set property cost reimbursement rates based on the value of the tangible assets alone. The new regulations were not applied in this case (37-8, 90-1).

The approval of the establishment of the Nursing Home by the Public Health Council (94) does not constitute approval of the purchase price as the cost basis for Medicaid reimbursement. The plain answer to that assertion is that the Council approves the establishment pursuant to Public Health Law § 2801-a and 10 N.Y.C.R.R. § 600.1; but only the Commissioner may certify Medicaid reimbursement rates under Public Health Law § 2807(3).

The Council is concerned with the need for and the ultimate feasibility of the health facility and it is to this end that it looks at the financial situation of a health facility. Here with 5% of revenues reflected in the total property

costs, disagreement about this one aspect of the rate would not bar its establishment. In approving this establishment of petitioner, the Council specifically referred to the solvency of the proposed owners not the profitability of their investment (94, p. 5):

> "It appears the applicants have the financial capability to consummate the acquisition and operate Sands Point Nursing Home."

Both state and federal courts have held that in dealing with an agent of the government, one is on notice of the limitation of his authority. In *United States* v. *R.C.A.*, 358 U.S. 334, 79 S. Ct. 457, 3 L.Ed. 2d 354 (1950), this Court held that an approval by the Federal Communications Commission of an exchange of stations did not bar an action by the Federal Government under the anti-trust laws. Although the FCC could take anti-trust considerations into account in approving licenses, it was not given the power to finally determine those issues. Thus its action could not prevent the enforcement of those laws by the Justice Department. *Id.* at 346, 351.

In *Matter of 225 E. 70th St. Corp.* v. *Weaver*, 6 N Y 2d 197, 189 N.Y.S. 2d 153 (1959), the New York Court of Appeals held that the State Rent Administrator had a right to revise rent increases previously granted for capital expenditures if the landlord had since obtained an abatement of taxes because of the same improvements. Judge Fuld stated that there was no representation, express or implied, that the rents could not be reduced and the statute warned of the scope of the Administrator's power. Here, too, no representations were made as to the effect of the Council's approval and the statute warned that Medicaid reimbursement rates were set by the Commissioner, only. The Commissioner's actions were triply reasonable (1) the rate sought by petitioner was on its face unreasonable; (2) the method of rate fixing used by the Commissioner was reasonable; and (3) no other rate or method of rate fixing was mandated by law.

II.

No important constitutional issues are presented in this petition.

As the discussion in Point I, indicates, the decisions of the courts below were supported by ample precedent and well within the requirements of the federal law. No new troublesome issue is presented in this petition. The assertion that "... this Court has not previously addressed itself to the broad and vital question of Medicaid reimbursement to skilled nursing facilities ..." (Pet'n, p. 13), does not present a reason for granting review by this Court. Petitioner fails to present an appropriate question. This Court does not sit to discuss "the availability of care to the categorically and medically needy" in the absence of a federal legal question of importance. The thrust of the petition is to seek review of State administrative procedures, but petitioner has had full opportunity to be heard in the appropriate forums—the State administrative and judicial tribunals.

Petitioner fails to demonstrate any denial of rights protected by the federal Constitution. The property component of its medicaid rate was reasonable and reasonably arrived at; which is to say that petitioner was accorded due process of law, contrary to its conclusory assertion. The only authority cited by petitioner, a 1932 Opinion of Mr. Justice Roberts from which Justices Holmes and Brandeis dissented, *Arizona Grocery Co.* v. *Atchison, Topeka & Santa Fe Ry. Co.*, 284 U.S. 370 (1932), was not based on a constitutional determination, but on an interpretation of the Interstate Commerce Act. This was specifically held by Mr. Justice Cardozo for a unanimous Court in *Great Northern Ry. Co.* v. *Sunburst Oil & Refining Co.*, 287 U.S. 358, 362-3 (1932):

> "*Arizona Grocery Co.* v. *Atchison, T. & S. F. Ry. Co.*, 284 U.S. 370, holds nothing to the contrary. This court in disposing of that case was not dealing with any question of constitutional law. It was construing a federal statute . . . The opinion of the court does not speak of the constitution, but plants itself upon the statute, and from that source and no other derives its energy."

In *Great Northern* this Court upheld as constitutional an interpretation of a State (Montana) statute which fixed railroad rates, but permitted them to be set aside by the State Board or a court if found to be unreasonable. Although that interpretation was rejected by the highest Court of Montana, it did not give retroactive effect to the decision, so that the retroactive rate adjustment in this case was held to be constitutional. This Court recognized the freedom of the States to experiment and change regulatory procedures (*Id.* at 363).

Great Northern, unlike *Arizona Grocery Co.*, is pertinent to this petition and disposes of it. Rate setting under the relatively new medicaid statute, in the 70's is like rate-setting for railroads was in the 20's and 30's—a developing field—where, experimentation and changes in federal and state policy based on experience, may be expected to occur.

III.

The decisions below were based on the particular facts of this rate fixing and are not likely to recur.

The decisions below were based on regulations which were changed a month after this facility was purchased by the present owners almost 6 years ago (10 N.Y.C.R.R. Part 86, for example §§ 86.21, 86.24, 86.29, 86.32). Petitioner alleges that it was "singled out" (Pet'n., p. 8) not to be reimbursed on the basis of purchase price. In defending his determination as being reasonable under the provisions of Public Health Law § 2807(3), Deputy Commissioner

McCann stated "This was the greatest increase in property costs from a sale of a nursing home I had seen" (86).

Since August, 1971, the methodology for determining the property cost component of nursing home rates in this situation has been set forth in detail in the regulations of the Department of Health since 1971 (10 N.Y.C.R.R. Part 86) so that petitioner's complaint has no importance for the future.

CONCLUSION

For these reasons, the petition for a writ of certiorari should in all respects be denied.

Dated: New York, New York, June 14, 1977

Respectfully submitted,

LOUIS J. LEFKOWITZ
Attorney General of the
State of New York
Attorney for Respondents

SAMUEL A. HIRSHOWITZ
First Assistant Attorney General

AMY JUVILER
Assistant Attorney General
of Counsel